

# Earning Review – Half Year 2021

## FFL: Positive developments and turnaround indicators

### Events

- Fauji Foods Limited (FFL PA) reported highest ever gross profit margin of 13.3% in 2QCY21 since its acquisition.
- Despite disruptions due to COVID-19 pandemic, we attribute this turnaround in gross profitability to management proactive approach for ensuring smooth procurement and distribution as the company has strong business continuity strategy.
- Efficient raw material procurement and recovery in UHT milk segment along with introduction of high margin products has led to higher sales. As a result, company reported growth of 35/39%YoY in sales during 1QCY21/1HCY21 versus during the same period last year.
- The above factors in our view culminated into improved performance as Fauji Foods Limited (FFL PA) reported gross profit of Rs282/Rs545mn in 1QCY21/1HCY21 compared to gross loss of Rs9/Rs109mn during the same period last year.
- Company's sales efficiency also increased as company's Selling and Distribution expense as portion of sales declined by 1.6/2.7ppt YoY in 2QCY21/1HCY21.
- FFL finance cost declined by 34% YoY in 2QCY21 due to capital restructuring through conversion of its parent company debt and 625bps cut in policy rate by SBP. To highlight, FFL has recently obtained shareholder approval for increase in its authorized capital to Rs18bn in order to facilitate further conversion of its parent company debt into equity.
- Subsequently, losses of the company reduced by 50%/57% YoY to Rs411/758mn in 1QCY21/1HCY21 when compared to loss of Rs828/Rs1,780mn in the same period last year.
- We attribute company's strong performance to (1) effective board leadership; changes in management; and result oriented corporate culture, (2) increased penetration in household retail segment, (3) enhanced sales contribution of high margin products, (4) efficient allocation of resources after management restructuring, (5) decline in finance cost due to capital restructuring and lower interest rates, and (6) abolishment of custom duty on import of skim milk powder in Federal Budget FY21.

### Outlook

- The stock is not in our formal coverage. However, we expect FFL to benefit from (1) favorable regulatory changes in FY22 budget, (2) further decline in finance cost due to parent company debt conversion, (3) increased contribution from butter and cheese products, (4) recovery in market share of UHT/tea whitener category, (5) introduction of high margin NURPUR dairy cream and (6) broadening of existing products variants as per customer preferences.
- However, emerging geopolitical situation, fourth wave of COVID, rising interest rates, PKR weakening and increasing input prices could be potential challenges for company's management.

#### Analyst

Foundation Research  
+92 21 3561 2290-94

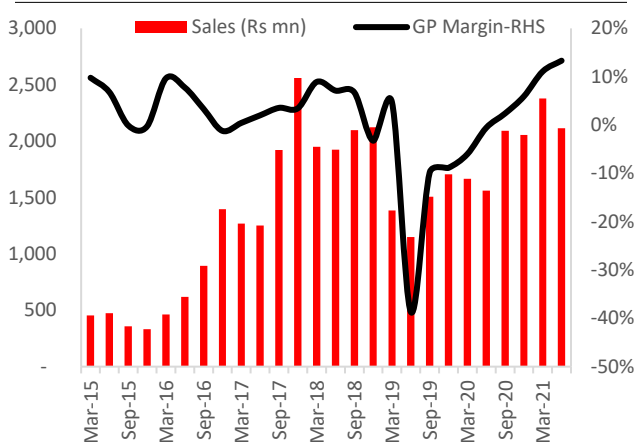
research@fs.com.pk  
Ext 312

**Table 1: FFL 2QCY21 Financial Highlights (Rs mn)**

Rs (mn)	2QCY21	2QCY20	YoY	QoQ	1HCY21	1HCY20	YoY
Net sales	2,115	1,562	35%	-11%	4,493	3,229	39%
COGS	1,834	1,571	17%	-13%	3,947	3,338	18%
<b>Gross profit</b>	<b>282</b>	<b>(9)</b>	na	7%	545	(109)	Na
S&D expense	269	223	21%	24%	487	436	12%
Admin expenses	96	91	6%	19%	176	183	-4%
Other income	24	12	100%	-36%	61	31	95%
<b>EBIT</b>	<b>(59)</b>	<b>(311)</b>	-81%	-2115%	(56)	(697)	-92%
Finance cost	319	483	-34%	1%	633	1,045	-39%
<b>PBT</b>	<b>(378)</b>	<b>(794)</b>	<b>-52%</b>	<b>22%</b>	<b>(689)</b>	<b>(1,742)</b>	<b>-60%</b>
Tax	33	34	-3%	-10%	69	39	79%
PAT	(411)	(828)	-50%	18%	(758)	(1,780)	-57%
<b>EPS@803.2mnsh</b>	<b>(0.51)</b>	<b>(1.03)</b>			<b>(0.94)</b>	<b>(2.22)</b>	
GP Margin	13%	-1%			12%	-3%	
Net Margin	-19%	-53%			-17%	-55%	

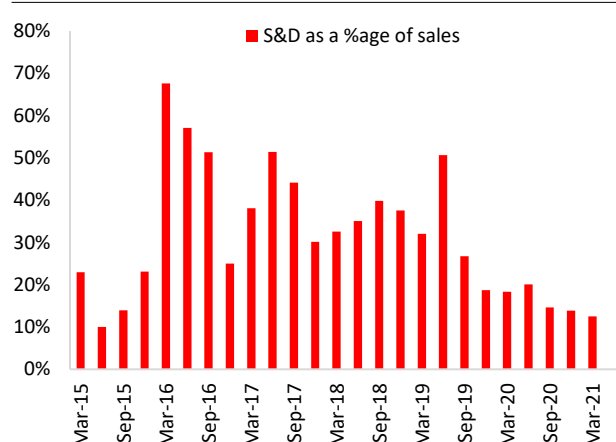
Source: Company Accounts, Foundation Research, July 2021

**Fig 1: FFL achieved highest ever gross margins**



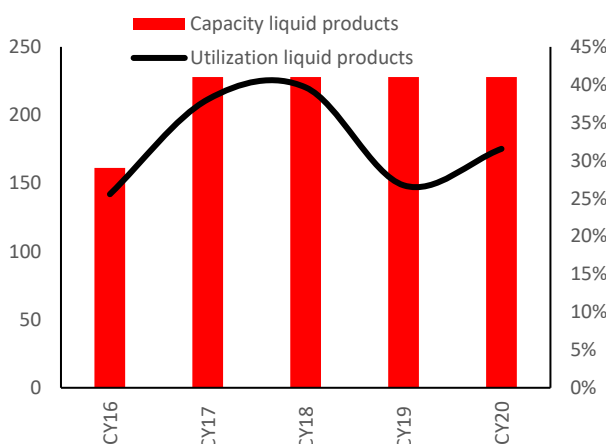
Source: Company Accounts, Foundation Research, July 2021

**Fig 2: with efficient management ...**



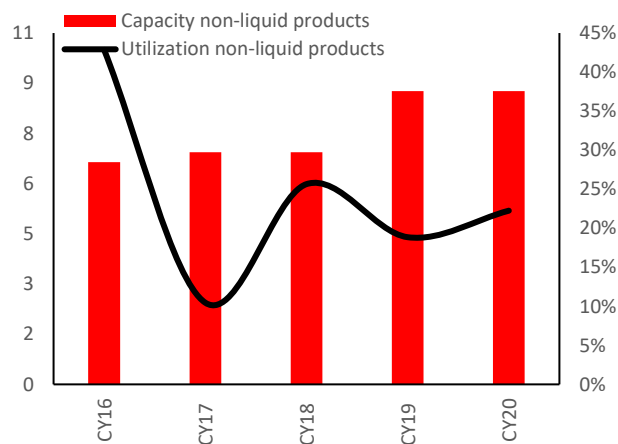
Source: Company Accounts, Foundation Research, July 2021

**Fig 3: ....capacity utilization aslo increased...**



Source: Company Accounts, Foundation Research, July 2021

**Fig 4: ..after change in management strategy (mn ltr)**



Source: Company Accounts, Foundation Research, July 2021

## Important disclosures:

**Disclaimer:** This report has been prepared by FSL. The information and opinions contained herein have been compiled or arrived at based upon information obtained from sources believed to be reliable and in good faith. Such information has not been independently verified and no guaranty, representation or warranty, express or implied is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. This document is for information purposes only. Descriptions of any company or companies or their securities mentioned herein are not intended to be complete and this document is not, and should not be construed as, an offer, or solicitation of an offer, to buy or sell any securities or other financial instruments. FSL may, to the extent permissible by applicable law or regulation, use the above material, conclusions, research or analysis before such material is disseminated to its customers. Not all customers will receive the material at the same time. FSL, their respective directors, officers, representatives, employees, related persons may have a long or short position in any of the securities or other financial instruments mentioned or issuers described herein at any time and may make a purchase and/or sale, or offer to make a purchase and/or sale of any such securities or other financial instruments from time to time in the open market or otherwise, either as principal or agent. FSL may make markets in securities or other financial instruments described in this publication, in securities of issuers described herein or in securities underlying or related to such securities. FSL may have recently underwritten the securities of an issuer mentioned herein. This document may not be reproduced, distributed or published for any purposes.

**Research Dissemination Policy:** Foundation Securities (Pvt.) Ltd. endeavors to make all reasonable efforts to disseminate research to all eligible clients in a timely manner through either physical or electronic distribution such as mail, fax and/or email. Nevertheless, not all clients may receive the material at the same time.

**Target price risk disclosures:** Any inability to compete successfully in their markets may harm the business. This could be a result of many factors which may include geographic mix and introduction of improved products or service offerings by competitors. The results of operations may be materially affected by global economic conditions generally, including conditions in financial markets. The company is exposed to market risks, such as changes in interest rates, foreign exchange rates and input prices. From time to time, the company will enter into transactions, including transactions in derivative instruments, to manage certain of these exposures.

**Analyst certification:** The views expressed in this research accurately reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the analyst(s) was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research. The analyst principally responsible for the preparation of this research receives compensation based on overall revenues of Foundation Securities and has taken reasonable care to achieve and maintain independence and objectivity in making any recommendations.

### Recommendations definitions

If	
Expected return >+10%	Outperform.
Expected return from -10% to +10%	Neutral.
Expected return <-10%	Underperform.